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FISCAL IMPACT REPORT

	ORIGINAL DATE 2/2/06		
SPONSOR <u>Lujan, B</u>	LAST UPDATED _____	HB <u>460</u>	
	MANUFACTURING CHEMICALS GROSS		
SHORT TITLE <u>RECEIPTS</u>		SB _____	
		ANALYST <u>Schardin</u>	

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY06	FY07	FY08		
	(7,980.0)	(8,220.0)	Recurring	General Fund
	(5,320.0)	(5,480.0)	Recurring	Local Governments

(Parenthesis () Indicate Expenditure Decreases)

SOURCES OF INFORMATION

LFC Files

Responses Received From

Taxation and Revenue Department (TRD)
Economic Development Department (EDD)

SUMMARY

Synopsis of Bill

House Bill 460 creates a gross receipts tax deduction for receipts from selling chemicals or reagents to a manufacturer for use in the manufacturing process if the manufacturer provides documentation to TRD that at least \$5 million has been spent on chemicals or reagents for use in the manufacturing process during the previous calendar year and delivers a nontaxable transaction certificate to TRD.

The effective date of these provisions is July 1, 2006.

FISCAL IMPLICATIONS

Citing the 2002 Economic Census of Manufacturing, TRD estimates that the tax base for this new deduction could be over \$200 million per year. Taxed at the statewide gross receipts tax rate of 6.6 percent, the bill would reduce revenue by about \$13.3 million per year. About 60 percent of this revenue reduction will accrue to the general fund, and about 40 percent to local governments.

SIGNIFICANT ISSUES

House Bill 460 attempts to reduce the tax burden on certain large-scale manufacturers caused by pyramiding, which results when transactional taxes such as New Mexico’s gross receipts tax are charged on the sale of business services from one business to another. As services are sold from one business to another in the course of production, the tax is levied multiple times and results in higher business costs and final product prices.

Pyramiding is a somewhat unique tax dilemma in New Mexico because the gross receipts tax is a fundamentally different structure than the sales tax used by most other states. While sales taxes are imposed on the buyer of consumer goods, the gross receipts tax is imposed on the seller of goods and services, whether that product is a finished good or an input used by another business.

Pyramiding affects some facets of New Mexico’s business community more than others. First, businesses that compete with other businesses outside of New Mexico may experience a competitive disadvantage because their competitors don’t pay multiple taxes on their inputs. Second, small businesses that contract with other businesses may experience a competitive disadvantage relative to larger firms. To exemplify this point, consider a small New Mexico firm that outsources its payroll function to another New Mexico firm. While this small business would pay gross receipts tax on its payroll services, a larger firm with its own payroll division would not pay gross receipts tax.

A gross receipts tax deduction is already available for receipts from selling chemicals or reagents for use in mining, milling or oil, or for sales in excess of 18 tons.

ADMINISTRATIVE IMPLICATIONS

TRD will experience moderate administrative impacts from House bill 460. TRD will develop nontaxable transaction certificates, prepare taxpayer education materials, train personnel, and develop audit and compliance procedures.

TECHNICAL ISSUES

The bill does not define the terms “chemical” or “reagent.”

OTHER SUBSTANTIVE ISSUES

TRD notes that although this measure will reduce the tax burden on manufacturers, its benefit could be offset if loss of revenue to the state leads to a higher tax rate on everything else.

TRD also notes that manufacturers currently benefit from several tax provisions such as Industrial Revenue Bonds, the investment credit (7-9A NMSA 1978), the high-wage jobs tax credit (7-9G-1 NMSA 1978) and the rural jobs tax credit (7-2E NMSA 1978).

SS/yr